

Department of Revenue

**For the Year Ended
June 30, 2000**

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STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
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John G. Morgan
Comptroller

September 5, 2001

The Honorable Don Sundquist, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and

The Honorable Ruth E. Johnson, Commissioner
Department of Revenue
1200 Andrew Jackson Building
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Department of Revenue for the year ended June 30, 2000.

The review of management's controls and compliance with policies, procedures, laws, and regulations resulted in certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/le



**STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT**

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September 5, 2001

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have conducted a financial and compliance audit of selected programs and activities of the Department of Revenue for the year ended June 30, 2000.

We conducted our audit in accordance with government auditing standards generally accepted in the United States of America. These standards require that we obtain an understanding of management controls relevant to the audit and that we design the audit to provide reasonable assurance of the Department of Revenue's compliance with the provisions of policies, procedures, laws, and regulations significant to the audit. Management of the Department of Revenue is responsible for establishing and maintaining internal control and for complying with applicable laws and regulations.

Our audit disclosed certain findings which are detailed in the Objectives, Methodologies, and Conclusions section of this report. The department's administration has responded to the audit findings; we have included the responses following each finding. We will follow up the audit to examine the application of the procedures instituted because of the audit findings.

We have reported other less significant matters involving the department's internal controls and/or instances of noncompliance to the Department of Revenue's management in a separate letter.

Sincerely,

Arthur A. Hayes, Jr., CPA, Director
Division of State Audit

AAH/le

State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
Department of Revenue
For the Year Ended June 30, 2000

AUDIT SCOPE

We have audited the Department of Revenue for the period July 1, 1999, through June 30, 2000. Our audit scope included a review of management's controls and compliance with policies, procedures, laws, and regulations in the areas of Management Information Systems, Processing, Taxpayer Services, Taxpayer Accounting, Revenue Accounting, Tax Enforcement, and compliance with the Financial Integrity Act. The audit was conducted in accordance with government auditing standards generally accepted in the United States of America.

AUDIT FINDINGS

Computer Programs Should Not Be Used To Change Data in RITS**

Computer programs called SPUFIs (Sequential Processing User File Input) are being used by Management Information Systems staff to correct taxpayer accounts directly in the Revenue Integrated Tax System (RITS) rather than through authorized and documented transactions (page 4).

The Department of Revenue Does Not Always Deposit Special Processing Remittances Timely*

Receipts are not always deposited timely. Special processing items were not deposited within 24 hours of receipt as required by state law (page 6).

Receipt and Deposit Dates of Payments Requiring Special Processing Are Not Always Recorded Correctly

The department does not record accurate receipt dates and deposit dates on RITS (page 7).

The Department Does Not Properly Track and Monitor Refund Claims in Order to Minimize Interest Paid**

Fifty-one of 60 refunds tested over \$50,000 took from 48 to 383 days to process before being turned over to the Attorney General's office for signatures. Nine of 61 refunds tested under \$50,000 exceeded the 45-day limit for refunding taxpayers to avoid paying an interest penalty (page 9).

**Balancing Problems Are Still Occurring
in RITS****

Out-of-balance conditions are occurring with the Revenue Integrated Tax System (RITS). The debits and credits of the Internal Tax Change columns did not balance 96% of the time (page 12).

**Tax Enforcement Delinquent Cases
Should Be Followed Up in a Timely
Manner****

In 21 of 60 delinquent tax enforcement cases tested, cases were not followed up in a timely manner (page 14).

* This finding is repeated from the prior audit.

** This finding is repeated from prior audits.

"Audit Highlights" is a summary of the audit report. To obtain the complete audit report, which contains all findings, recommendations, and management comments, please contact

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**Audit Report
Department of Revenue
For the Year Ended June 30, 2000**

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Department of Revenue For the Year Ended June 30, 2000

INTRODUCTION

POST-AUDIT AUTHORITY

This is the report on the financial and compliance audit of the Department of Revenue. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

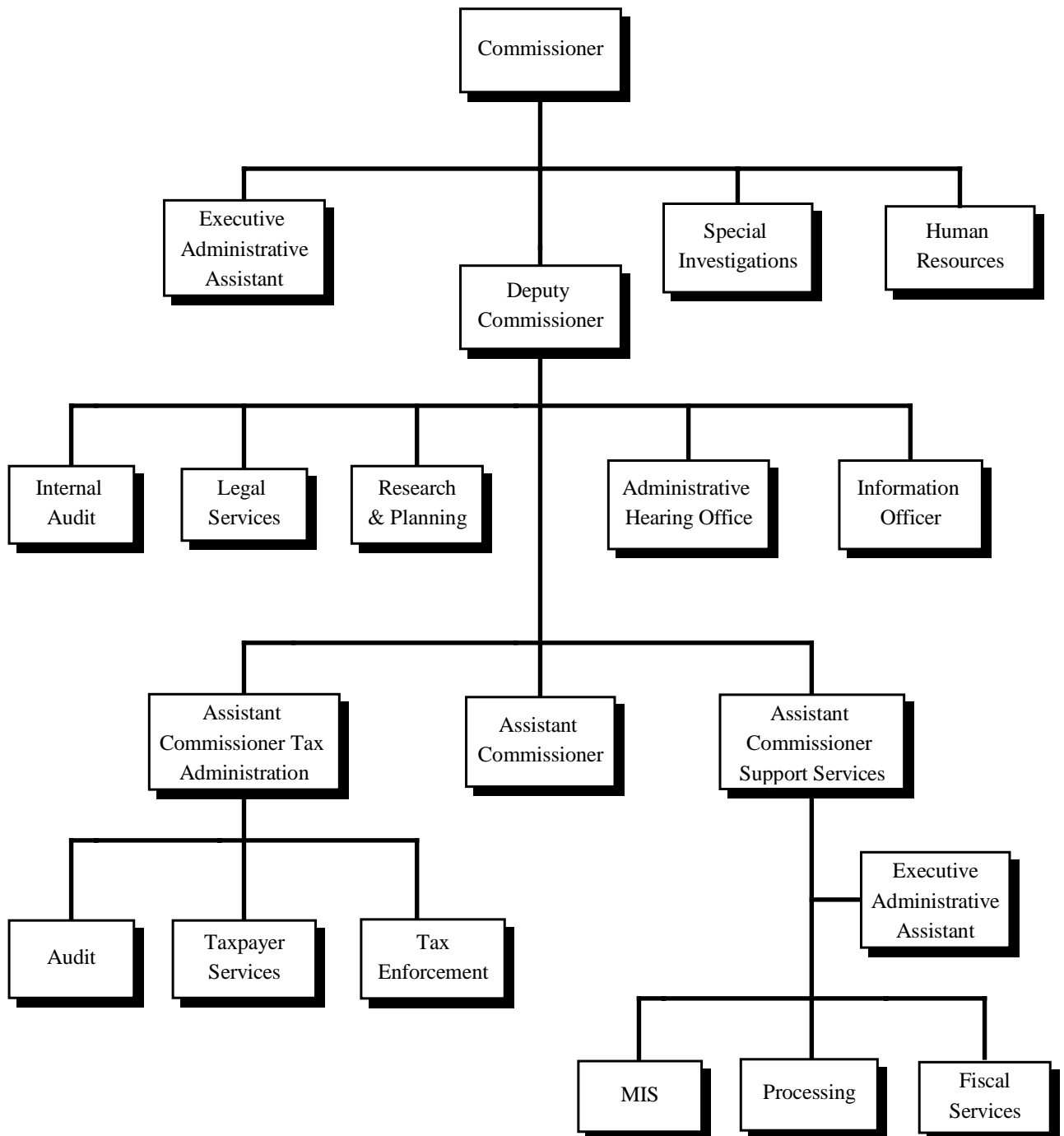
The mission of the Department of Revenue is to collect state revenue. Specifically, the department is responsible for the collection of most state taxes and fees, for enforcing the revenue statutes of the state to ensure that taxpayers are in compliance with all tax laws, and for preparing the monthly apportionment of revenue collections for distribution to various state funds and local units of government. The department also offers taxpayer assistance and taxpayer education. In an effort to perform its duties, the department has divided these functions into six divisions: Fiscal Services, Tax Enforcement, Management Information Systems, Taxpayer Services, Audit, and Processing.

An organization chart of the department is on the following page.

AUDIT SCOPE

We have audited the Department of Revenue for the period July 1, 1999, through June 30, 2000. Our audit scope included a review of management’s controls and compliance with policies, procedures, laws, and regulations in the areas of Management Information Systems, Processing, Taxpayer Services, Taxpayer Accounting, Revenue Accounting, Tax Enforcement, and compliance with the Financial Integrity Act. The audit was conducted in accordance with government auditing standards generally accepted in the United States of America.

TENNESSEE DEPARTMENT OF REVENUE



PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The Department of Revenue filed its report with the Department of Audit on February 1, 2001. A follow-up of all prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDINGS

The current audit disclosed that the Department of Revenue has corrected previous audit findings concerning Management Information Systems policies and procedures manuals, recording new corporations in RITS, disbursements to other states for International Registration Plan Taxes, and controls over diaries in the Tax Enforcement Division.

REPEATED AUDIT FINDINGS

The prior audit report also contained findings concerning controls over changes to RITS data, timely deposit of remittances, timely processing of refunds, out-of-balance situations, and timely follow-up of Tax Enforcement cases. These findings have not been resolved and are repeated in the applicable sections of this report.

OBJECTIVES, METHODOLOGIES, AND CONCLUSIONS

MANAGEMENT INFORMATION SYSTEMS

Our objectives in reviewing the Management Information Systems (MIS) division were to determine whether

- relevant policies and procedures had been placed in operation;
- computer resources were planned, managed, and utilized effectively;
- an adequate disaster recovery plan had been implemented;
- user access to the Revenue Integrated Tax System (RITS) was adequately controlled;
- RITS application documentation was complete; and
- adequate controls were in place over RITS program changes.

We examined the policies and procedures manuals to determine if policies and procedures were current and reflected existing operational conditions. To determine if computer resources were managed appropriately, we reviewed the minutes and purpose of the Management Advisory Committee and reviewed the three-year plan. We also interviewed key personnel and reviewed the disaster recovery plan to determine that it had been implemented and was current. In addition, we reviewed individuals with Resource Access Control Facility (RACF) special access and verified that passwords were changed on a regular basis, and we reviewed access of terminated employees and dataset protection. To determine if user access to RITS was adequately controlled, we also tested a nonstatistical sample of users for proper access to RITS screens. We interviewed key personnel and reviewed RITS documentation to determine if the system was adequately documented. Also, we tested nonstatistical samples of Sequential Processing User File Inputs (SPUFIs) and program changes to determine if adequate controls were in place.

As a result of our review, we determined that relevant policies and procedures were placed into operation, computer resources were utilized effectively, and an adequate disaster recovery plan was in place. Also, RITS application documentation was complete and user access was adequately controlled. We found that SPUFIs were still being used to correct data in RITS. In addition to the finding, other minor weaknesses were reported to management in a separate letter.

1. Computer programs should not be used to change data in RITS

Finding

As stated in the prior three audits, computer programs called SPUFIs (Sequential Processing User File Input) are being used by Management Information Systems (MIS) staff to correct taxpayer accounts directly in the Revenue Integrated Tax System (RITS) rather than through authorized and documented transactions. Management concurred, stating that “the division is continually working to correct the problems causing these errors so that the need for SPUFIs is minimized.” Although some of the problems have been corrected, SPUFIs are still being used to change data. Making changes directly to the system with a SPUFI, instead of correcting errors through transactions, circumvents the controls the system is designed to provide, leaving no audit trail for management to determine the activity in an account.

Also, although OIR programmers normally execute these types of programs, MIS analysts are the individuals who run the SPUFIs on production data. Analysts are responsible for program design, and allowing them to change production data could compromise taxpayer accounts.

Recommendation

The system should be corrected to process transactions properly so that the use of SPUFIs is not necessary. Analysts should not have access to make data changes.

Management's Comment

We concur. The department continues to work through the Information Technology Resources Division (ITR) and through Office of Information Resources (OIR) toward the resolution of identified problems in RITS. In addition, ITR strives to develop and implement new and enhanced production jobs with features designed for users to accomplish large volumes of work without ITR intervention.

The results of the ongoing efforts by ITR and OIR to eliminate system problems can be measured by the dramatic decrease in the number of update SPUFIs run in the last year. At the end of the fiscal year 1999/2000, there were 838 entries in the Data Fix Log. At the end of the fiscal year 2000/2001, there were 250 entries.

Currently, OIR Data Base Administration (DBA) personnel and ITR manager, in the absence of OIR DBA personnel, have the authority to run production update SPUFIs when requested and approved in accordance with the written data fix procedures. While the use of SPUFIs has substantially decreased, the use of update SPUFIs probably will not be entirely eliminated. They are used to correct error conditions that cannot be resolved through normal processing or for large volume situations where resolution would place undue burden on the users; however, the department will continue efforts to minimize the use of production update SPUFIs.

PROCESSING DIVISION

Our objectives in reviewing the Processing Division were to determine whether

- policies and procedures that affect each unit of the Processing Division had been identified,
- funds received by the Processing Division were properly safeguarded and deposited in a timely manner,
- policies regarding date stamps and envelope retention were followed,
- remittances were being properly recorded by the Exceptions Processing Unit, and
- the Exceptions Processing Unit adequately safeguarded funds and made deposits in a timely manner.

We interviewed key personnel to gain an understanding of the division's policies and procedures. We observed the process of safeguarding revenue received and discussed the process with the appropriate personnel. To determine if deposits were made timely and recorded accurately by the Processing Division and the Exceptions Processing Unit, we tested

nonstatistical samples of cash receipts. In addition, we tested a nonstatistical sample of returns for date stamps and envelope retention.

As a result of our testwork, we determined that funds were appropriately safeguarded and that policies regarding date stamps and envelope retention were followed. We found that deposits were not always being made timely and there were problems with recording receipt dates and deposit dates on RITS.

2. The Department of Revenue does not always deposit special processing remittances timely

Finding

As noted in the prior audit, the department does not always deposit receipts timely. Management concurred with the prior finding, stating, “A review of the unit’s operational procedures relating to the deposit of remittances revealed deficiencies which were immediately corrected by division management.” Based on follow-up work performed, improvement was made in this area. However, 3 of 27 receipts received by the exceptions processing unit in February 2001 (11%) were not deposited within 24 hours as required by state law. The three items totaling \$28,020.52 were deposited 2 and 3 business days late. Also, 57 of 71 receipts that were deposited to the suspense account during the audit period (80%) were not deposited timely. The related dollar amount of \$390,844.22 was deposited from 1 to 18 days late. The department receives tax returns and payments that are not processible in the original form in which they were received or that have other special handling requirements. For these items, the Exceptions Processing Unit either obtains the information necessary to complete processing or forwards a copy of the payment and related support to the appropriate tax section for follow-up. While the processing or follow-up occurs, the payment should be deposited immediately. Section 9-4-301(a), *Tennessee Code Annotated*, states:

It is the duty of every department, institution, office and agency of the state and every officer and employee of state government, including the state treasurer, collecting or receiving state funds, to deposit them immediately into the treasury or to the account of the state treasurer in a bank designated as a state depository or to the appropriate departmental account.

The Department of Finance and Administration defines the term “immediately” in Section 9-4-301 as follows:

For departments, institutions, offices and agencies within 5 miles of a state depository, “immediately” means the same day.

When receipts are not deposited immediately as required by state law and recorded in the suspense account, the risk of loss or misappropriation increases, and interest income is lost.

Recommendation

The Department of Revenue management should assign specific responsibility to ensure that all payments requiring special processing are deposited in the suspense account within 24 hours.

Management's Comment

We concur. Processing of these payments is outside the general workflow because sufficient information for processing is not received or the payment must be distributed to the proper account(s) in some restricted manner, such as payments for Bankruptcy, Special Investigations, or Field Audit.

After the last audit report, improvements were made in the processing procedures addressing the timely deposit of funds; however, additional weaknesses were revealed in this year's review requiring the implementation of stronger controls to ensure the deposit of these remittances within 24 hours from the time received. The division immediately implemented a date stamping procedure for all payments processed through the Exception Processing Unit. The date stamp reflects the date that the item was received by the division and provides the supervisory staff with a means to track the timeliness of processing. In addition, the Processing Division is meeting with the other divisions that collect payments from taxpayers to coordinate activities across divisional lines to expedite the processing of payments and ensure that all requirements are met.

3. Receipt and deposit dates of payments requiring special processing are not always recorded correctly

Finding

The department does not ensure that accurate and consistent receipt dates and deposit dates are recorded on the Revenue Integrated Tax System (RITS) and other internally created supporting documents for taxpayer payments. Twenty-one of 27 exception payments tested that were received on February 20, 2001, (78%) had incorrect receipt or deposit dates recorded in RITS. Exception payments are payments that are not processible in the original form in which they are received or that have other special handling requirements. While they are investigated, the payments are deposited in the suspense account. For taxpayer payments that were suspended for the period September 2000 through October 2000, 63 of 71 receipt or deposit dates (89%) were not consistently recorded in RITS and on supporting documentation.

The department does not use the actual receipt date to record the receipt of payments. Sometimes staff record the actual date of receipt on the system-generated remittance. However, at other times, staff record the date of the check, the postmark date on the envelope, or the date of receipt stamped on the remittance. Occasionally staff record the date that the internal remittance

document was created. In three cases, staff recorded a deposit date that was earlier than the receipt date that was recorded. Regarding the deposit date, apparently updates made to RITS sometimes alter the recorded deposit date of a payment.

The inconsistent and inaccurate receipt and deposit dates make it difficult to determine if the deposit of the payments was made timely and if the payment was applied to the taxpayer account.

Recommendation

The Department of Revenue should immediately adopt a policy to ensure that the actual receipt dates and deposit dates are recorded on RITS and on all internally created documentation used to support and track the receipt of taxpayer payments.

Management's Comment

We concur. Management from the Processing, Taxpayer Services, Tax Enforcement, Audit and Information Technology Resources Divisions met to discuss the issues presented in the finding. The department will work to develop and implement a policy addressing consistency and accuracy of the RITS receipt and deposit dates in the processing of documents and remittances.

TAXPAYER SERVICES

Our objectives in reviewing Taxpayer Services were to determine whether

- certain rules, regulations, and laws that affect taxpayer registration had been identified;
- taxpayer applications for registration for the audit period had been correctly coded and processed;
- refunds were to valid taxpayers;
- the section's managerial controls over corrections and changes to taxpayer account balances in the Revenue Integrated Tax System (RITS) were effective; and
- the procedures for adding and deleting taxpayer accounts were proper.

We interviewed key personnel to gain an understanding of the department's procedures and compliance with rules and laws. We identified and reviewed certain rules, regulations, and laws that affect taxpayer registration. In addition, we selected a nonstatistical sample of refunds and verified existence of taxpayers. We reviewed employees having access to make corrections

and changes to taxpayers' accounts on RITS for proper authorization, and we also reviewed error reports. To determine if corporations were properly recorded or properly removed, we tested nonstatistical samples of new corporations and deleted corporations from the Secretary of State's office and traced these entities to the taxpayers listed on RITS.

Based on our work, we determined that refunds were made to valid taxpayers and that procedures for adding and deleting taxpayer accounts are proper. We found that controls over changes to taxpayer account balances were effective.

TAXPAYER ACCOUNTING

Our objectives in reviewing Taxpayer Accounting were to determine whether

- controls over the refund process for taxpayer accounting were adequate;
- refunds had been reviewed, properly approved, and recorded to the correct taxpayer account;
- transactions and conversation screens were secure from unauthorized use;
- reconciliations were performed and are properly reviewed; and
- State of Tennessee Accounting and Reporting System (STARS) and Revenue Integrated Tax System (RITS) refunds reconciled.

We interviewed key personnel to gain an understanding of the department's procedures and controls in the refund unit, and we tested nonstatistical samples of refunds for proper review, approval, accounting entries, and timeliness. We reviewed security over access to RITS, and we reviewed reconciliations for proper review and to ensure that RITS is reconciled to STARS.

As a result of our testwork, we determined that refunds were reviewed, approved, and recorded to the correct accounts. The refunds were reconciled appropriately between STARS and RITS. We also determined that transactions and conversation screens were secure from unauthorized use. However, we found that refunds were not being processed timely. In addition to the finding, a minor weakness was reported to management in a separate letter.

4. The department does not properly track and monitor refund claims in order to minimize interest paid

Finding

As noted in the prior two audits, the department does not properly monitor timeliness of individual refund claims to prevent excess interest being paid. Management concurred with the prior finding stating, "The supervisors in the unit will continue to monitor the age of refunds assigned to the unit and will work to minimize any delays." However, the current audit revealed

that 51 of 60 refunds tested over \$50,000 (85%) took from 48 to 383 days to process in the Refund and Penalty-Waiver Unit before being sent to the Attorney General's office for signatures. Nine of 61 refunds tested under \$50,000 (15%) exceeded the 45-day limit for refunding taxpayers to avoid paying an interest penalty.

The Refund and Penalty-Waiver Unit is still not closely monitoring refunds to ensure that they are sent through the signature process and to ensure payment is made within 45 days of the claim date, which is the date on which the Refund and Penalty-Waiver Unit establishes a refund claim as a valid refund. The department still has not established procedures to ensure that a refund is sent through the signature process and refunded within 45 days as required by state law. Section 67-1-801(b), *Tennessee Code Annotated*, states:

When it is determined by administrative review or court that any person is entitled to a refund or credit of any tax collected or administered by the commissioner, interest shall be added to the amount of refund or credit due, beginning forty-five (45) days from the date of filing a claim for refund.

When refunds are not processed within 45 days of the claim date, the state is assessed interest on the refund amount. Of the 60 refunds that took more than 45 days to process, interest was only paid for 30 of the refunds. If these 30 refunds were processed timely, the state could have saved a minimum of \$95,702.94 in interest.

Recommendation

The department should establish procedures for tracking and monitoring refund claims. These procedures should be adequate to ensure that the refund will be approved and will have all required signatures within 45 days to comply with statute. The refund tracking should be used to evaluate the process and to ensure the refund does not remain in one area for an excessive amount of time.

Management's Comment

We concur in part. The Refunds and Penalty Waivers Unit does have a tracking system and a procedure in place to monitor and track refunds assigned to the unit and to track the amount of interest paid on all refunds. However, we are currently revising the system and the procedure to better identify areas where processing delays are observed. As a result of these revisions, the supervisors in the unit will be better able to monitor the age of refunds and minimize any delays.

It should be noted, however, that the department will not issue a refund that has not been determined as valid to avoid paying interest. The amount by which original claims for refund are reduced as a result of audit efforts dwarfs the amount of interest paid on the refunds ultimately approved and processed. Of the 24 refunds in the sample that the department paid interest on,

nine (38%) refunds were reduced by a total of \$10,433,889.13 from the original amounts requested by the taxpayers compared to the \$95,702.94 of interest paid (interest paid on these claims is less than 1% of the tax dollars recovered through audit efforts).

In addition, the department established a strategy in the Strategic Plan dated April 12, 2001, specifically addressing the improvement and monitoring of the refund processing activities. To evaluate the processes and the success of changes made in refund processing, a performance measure was established requiring periodic reporting of interest paid by tax type and signatory threshold. This information will be valuable in the department's endeavors to expedite refund processing.

Auditor's Comment

We recognize that it may occasionally be beneficial to the state to delay a refund to reduce the amount paid to the taxpayer. However, the rate of occurrence noted in the finding seems to indicate that delays occur frequently. Every effort should be made to process refunds in the most expeditious manner in order to minimize the amount of interest paid.

REVENUE ACCOUNTING

Our objectives in reviewing the Revenue Accounting section were to determine whether

- certain rules, regulations, and laws that affect tax revenues had been identified;
- the cashier's Daily Summary of Collections Report was being properly completed;
- deposit slips were reconcilable to the Bank Deposit Report, the Daily Summary of Collections Report, and the Daily Balancing Report;
- revenues had been properly recorded and classified by tax type in the monthly collection reports;
- reconciliations were being performed and were properly documented;
- error reports were used to ensure errors were corrected properly;
- procedures used for monthly close-outs were proper; and
- procedures used to reallocate undistributed funds for the Revenue Integrated Tax System (RITS) were proper.

We interviewed key personnel and reviewed applicable sections of *Tennessee Code Annotated* to identify laws that affect tax revenues. We also reviewed the cashier's Daily Summary of Collections Report for completeness. We performed testwork to determine that deposit slips were reconcilable to the Bank Deposit Report, the Daily Summary of Collections Report, and the Daily Balancing Report. To determine revenues were properly recorded and

classified by tax type in the monthly collection reports, we performed analytical procedures. In addition, we reperformed reconciliations and reviewed reconciling items, and we tested bank errors for proper corrections. We reviewed monthly closeouts and reconciled the RITS Daily Summary of Collections to the County Situs Report, and we reviewed procedures for reallocating undistributed funds to determine whether those procedures were proper.

As a result of our testwork, we determined that the Daily Summary of Collections Report was properly completed, deposit slips reconciled to the applicable reports, reconciliations and error reports were utilized appropriately, and closeout procedures and reallocation procedures were proper. We also determined that revenues had been properly recorded and classified by tax type in the monthly collection reports. However, we found that balancing problems were still occurring in RITS.

5. Balancing problems are still occurring in RITS

Finding

As noted in the prior three audits, balancing problems are still occurring in the Revenue Integrated Tax System (RITS) accounting reports. Processing errors occur that cause differences in the debits and credits of the Internal Tax Change columns, creating an out-of-balance condition. Out-of-balance conditions can occur when the taxes are moved around in the system internally because of line-item adjustments, transfers, refunds, bad checks, conversion to RITS, and system problems. When the out-of-balance conditions are identified, department personnel must research the cause and make appropriate corrections. Management concurred with the prior finding and stated that program changes have been made in both Taxpayer Accounting and Revenue Accounting to resolve some of the major balancing issues. However, from July 1, 1999, to June 30, 2000, Department of Revenue financial reports were out-of-balance 237 days out of 248 days, or 96% of the time. This represented an increase from the prior year when the out-of-balances occurred 87% of the time. The system should be designed to minimize these conditions and to lessen the need for the labor-intensive error corrections.

Recommendation

The commissioner should review the program changes made to resolve RITS out-of-balances, identify the conditions that are still causing out-of-balances, and ensure that proper measures are implemented as quickly as possible to prevent those conditions.

Management's Comment

We concur. Program changes made to Taxpayer Accounting and Revenue Accounting to resolve some of the major balancing issues were moved to production in August 2000. From

September 1, 2000, through June 30, 2001, RITS financial reports were out of balance 63 days of 213 (29.58%).

Out-of-balance situations are corrected each month prior to closeout for that month. The department will continue its efforts to address the balancing problems in RITS.

TAX ENFORCEMENT DIVISION

For the Tax Enforcement Division, our objectives were to determine whether

- the division complied with rules and regulations of the department and the applicable *Tennessee Code Annotated* sections;
- regional Tax Enforcement offices were mailing receipts to the department's mail room timely, and the receipts were deposited by the department timely;
- the classification of delinquent RITS accounts as dormant, pending dormant, or unenforceable was properly supported and approved;
- bankruptcy claims were filed timely by the department, and the claims were properly computed and tracked by the department;
- the division was attempting to collect current delinquencies in a timely manner and following the appropriate collection procedures;
- Tax Enforcement officers' receipt books and diaries were properly completed and reviewed by their supervisors;
- cash received by Tax Enforcement officers was deposited at a local bank timely; and
- Tax Enforcement officers' diaries were properly completed and reviewed by their supervisors.

We interviewed key personnel, and we reviewed Tax Enforcement's procedures manual and the applicable *Tennessee Code Annotated* sections to determine if the Tax Enforcement Division is in compliance with rules and regulations. We also performed testwork on a nonstatistical sample of receipts to determine if they were deposited in a timely manner. To determine if classifications of dormant, pending dormant, or unenforceable were properly supported and approved, we tested a nonstatistical sample of RITS accounts classified as such. We tested a nonstatistical sample of bankruptcy claims to determine if proper and timely action was taken to collect funds, and we performed testwork on nonstatistical samples of receipt books and diaries for completeness and review. In addition, we tested a nonstatistical sample of delinquent cases to determine if the status was appropriately approved and follow-up was timely.

As a result of our testwork, we determined that the Tax Enforcement Division is in compliance with rules and regulations regarding cash receipts, delinquent accounts, bankruptcy

claims, collections, receipt books, and diaries. However, we found that delinquent cases were not being followed up in a timely manner. In addition to the finding, other minor weaknesses came to our attention, which have been reported to management in a separate letter.

6. Tax Enforcement delinquent cases should be followed up in a timely manner

Finding

As noted in the two prior audits, the Tax Enforcement Division is not following up on delinquent cases in a timely manner. Management concurred with the prior finding stating, “With a full staff in the unit, division management continues to review and implement procedures and methods to work these cases more quickly.” However, documentation in the Revenue Integrated Tax System (RITS) showed that 21 of 60 delinquent tax enforcement cases tested (35%) were not followed up in a timely manner. The case history screen in RITS shows no action was taken on these cases from 4 to 12 months. Chances of collecting revenue decrease when an account is not followed up regularly.

Recommendation

Supervisors and regional managers should implement procedures for tracking cases to ensure that all cases are followed up in a timely manner.

Management’s Comments

We concur. Nineteen of the 21 cases identified were out-of-state accounts. While the staffing of the Out-of-State Unit has not increased since the last audit, the average caseload per officer has been significantly reduced from 1,104 cases for the fiscal year 1999-2000 to 647 cases during the fiscal year 2000-2001. Supervision and monitoring of the cases are primarily responsible for this change.

Division management is currently working on supervisor’s and manager’s procedures manuals. The issue of timely case follow-up will be addressed in those manuals. In addition, the department is in the process of implementing the predictive dialer program to provide a more timely contact with taxpayers for collection of delinquent taxes.

FINANCIAL INTEGRITY ACT

Section 9-18-104, *Tennessee Code Annotated*, requires the head of each executive agency to submit a letter acknowledging responsibility for maintaining the internal control system of the agency to the Commissioner of Finance and Administration and the Comptroller of the Treasury by June 30, 1999, and each year thereafter. In addition, the head of each executive agency is also

required to conduct an evaluation of the agency's internal accounting and administrative control and submit a report by December 31, 1999, and December 31 of every fourth year thereafter.

Our objective was to determine whether the department's June 30, 2000, responsibility letter was filed in compliance with Section 9-18-104, *Tennessee Code Annotated*.

We reviewed the June 30, 2000, responsibility letter submitted to the Comptroller of the Treasury and to the Department of Finance and Administration to determine adherence to the submission deadline, and we determined that the Financial Integrity Act responsibility letter was submitted on time.

OBSERVATIONS AND COMMENTS

TITLE VI OF THE CIVIL RIGHTS ACT OF 1964

Section 4-21-901, *Tennessee Code Annotated*, requires each state governmental entity subject to the requirements of Title VI of the Civil Rights Act of 1964 to submit an annual Title VI compliance report and implementation plan to the Department of Audit by June 30, 1994, and each June 30 thereafter. The Department of Revenue filed its compliance report and implementation plan on June 30, 2000.

Title VI of the Civil Rights Act of 1964 is a federal law. The act requires all state agencies receiving federal money to develop and implement plans to ensure that no person shall, on the grounds of race, color, or origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal funds.

On October 15, 1998, the commissioner of Finance and Administration notified all cabinet officers and agency heads that the Human Rights Commission is the coordinating state agency for the monitoring and enforcement of Title VI.

A summary of the dates state agencies filed their annual Title VI compliance reports and implementation plans is presented in the special report *Submission of Title VI Implementation Plans*, issued annually by the Comptroller of the Treasury.

APPENDIX

Department of Revenue divisions and allotment codes:

347.01	Administration
347.02	Tax Enforcement
347.11	Management Information Systems
347.13	Taxpayer Services
347.14	Audit Division
347.16	Processing Division